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IF YOU CAN'T BEAT THEM, SUPPORT THEM: WHY SUSTAINING INFORMAL ENTERPRISES IS KEY TO PROMOTING DECENT WORK.

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If you can't beat them, support them: Why sustaining informal enterprises is key to promoting decent work.

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Author

Pablo Navarette

Pablo holds an Architecture Degree (equivalent to RIBA parts 1, 2 and 3) from the Universidad de Chile. He also achieved a double MSc in Urban Policy at Sciences-Po Paris and the London School of Economics (LSE). At the Universidad de Chile, Sciences-Po Paris and LSE, Pablo deepened his interest in and knowledge of urban planning, public policies and urban informal economy. In particular, for his MSc dissertation he focused on scavenging and urban recycling in Santiago of Chile.

Pablo is currently Adjunct professor at Universidad San Sebastian in Chile and a PhD candidate in Regional and Urban Planning at the LSE. Pablo has widened his research on informal economy and public policies, focusing not only on scavenging butalso on street markets and home-based enterprises. He presented his research at the 2015 Academy ofEconomics and Finance conference in Jacksonville (Florida),being awarded the first prize for the best paper inEconomics. In 2015, he has also beenawarded one out of the three "Strictly Come Researching"prizes for PhDstudents at the LSE Research Festival (seePablo's interviewwith Professor Conor Gearty). In 2016, his research onsocial housing, co-authored with Nicolas Navarrete, was awarded a prestigious prize from

the Development Bank of Latin America (CAF) for their international competition "Habitat and Urban Development". Only five proposalswere awarded a prize from a total 252 entries. At LSE,Pablo has taught GY140: Methods in Spatial and SocialAnalysis and GY240: Research Techniques (Spatial, Socialand Environmental).

Before undertaking PhD research, Pablo worked as an architect and urban planner in the local and central government. In particular, he worked as an architect for the Ministry of Housing and Urban Development of Chile and the Atelier Jean Nouvel, as a town planning consultant for a Council of the Santiago Metropolitan Region and as a planner for the Ministry of Transport of Chile. In addition, in 2013, Pablo took part in the presidential campaign of Michelle Bachelet, leading the housing and planning sections of the manifesto proposed by President Bachelet. His proposals were the basis for a number of policies implemented by the Ministries of Housing and Urbanism, Economy, Environment and Public Land.

Abstract

The Informal Economy (IE) constitutes two-fifths of the total national GDP in developing countries, and provides employment for two out of every three people worldwide, making it the largest source of employment for the most vulnerable people in society. There is also an increasing recognition that the IE is going to persist in the long term. On the basis of research on three informal sub-sectors in Santiago de Chile, this policy paper argues that governments should strongly support the economic growth of informal enterprises to contribute to the achievement of the decent work objectives stated in the UN's 2030 Sustainable Development Goals. These cases show that public policy can increase the productivity of informal enterprises, resulting in higher salaries and enhanced working conditions. Support for informal enterprises should be focused on overcoming four "poverty traps" that inhibit the improvement of these businesses. This requires a rethinking of development policies, moving away from policies that combat informality, towards ones that embrace and build on its natural strengths.

The research

In this report, I analyse three informal economic sub-sectors of Santiago de Chile – waste-picking, street vendors and home-based enterprises (HBEs) – that together represent a large share of employment in the city. I interviewed 99 informal workers and local authority representatives to understand the diverse policy rationale of local authorities and the impact of municipal policies on working conditions in the IE. These results are generalised over the larger population using 904 representative surveys, two randomised surveys (in the case of HBEs and street vendors) and a census of four waste-picker cooperatives. Local governments in the region have a high degree of independence that allow them to create and implement policies on a local level, and so I have been able to analyse a diverse range of strategies and approaches toward the IE.

Redefining the role of the informal economy on the 'decent work' objective

> A: We can increase the efficiency, expand the production and in turn improve the quantity and quality of (informal) employment, but we need more aggressive policies of support… This is what we are trying to do. Waste-picking can be an evolutionary process…from an informal activity, to micro-entrepreneurship and (full-scale) entrepreneurship.

Public officer, Municipality of Peñalolén

The UN has recently cited an end to poverty and the creation of decent work as objectives of its Sustainable Development Goals for 2030, putting the quantity and quality of work at centre stage of international development discussions (UN 2015). Although 900 million people in urban areas of developing countries depend on the IE for their livelihood, it has traditionally been characterised as having low productivity, low wages and poor working conditions. The IE has thus been perceived as a significant impediment to the creation of decent work on a global scale. This has lead to more than four decades of policy interventions with the ultimate aim of making the IE disappear. In spite of the opposition it has faced, the IE has remained, and even expanded, over time.

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Since the term "informal sector" was first coined in 1972, we have passed through several waves of international and national poverty alleviation policies. In the 1970s, the IE was faced with direct repression and policing (Bangesser 2000, p.4); through the 1980s, calls were made for the extension of social protection policies to include informal workers exploited through subcontracting arrangements (Centeno & Portes 2006); in the 1990s, tolerance and actions to formalise informal enterprises were taken in an attempt to reduce its size (de Soto 1989); and finally, in the early 2000s, policies reverted to their previous aim of eliminating the IE using a combination of repressive actions and formal job creation reforms (Maloney 2004, Perry et al. 2007). Contrary to the objectives of these policies, it is estimated that the IE provides and will continue to provide more employment worldwide than the formal economy does (OECD 2009a, p.2, ILO 2013, p.31). At this point, it is clear that "the informal economy is here to stay" (Chen et al. 2001, p.iii). With this in mind, it is in the best interest of international development agencies that working conditions in the informal economy reach their highest possible standard.

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So, how do we follow four decades of unsuccessful policies that have, more often than not, been aimed at the elimination of the informal economy? In recent years, academics have used terms such as "co-production", "inclusive growth" or "hybrid economy" to describe a recent tendency in development policies that move from working against to working with informal enterprises (Joshi & Moore 2004, Chen 2015). Waste-pickers have formed organisations and are being integrated into waste management services provided by city councils in Cairo (Egypt) and Belo Horizonte (Brazil) (Fergutz et al. 2011, Kingsley 2014). Street food vendors have been merged into traditional street markets and receive stalls with access to clean water in Durban (South Africa) and Dar es Saalam (Tanzania) (FAO. 2003, Skinner 2008). HBEs are receiving houses in good locations and specialised house-spaces in Nairobi (Kenya) (Kigochie, 2001). Providing this kind of support can generate high improvements in productivity, and brings this informal employment closer to having decent working standards.

I will now focus on five Chilean municipalities – Santiago, Lo Prado, La Reina, Macul and Peñalolén – that have integrated innovative practices into their policy approaches. I have identified four general policy types that are effective in improving working standards in the IE, and the rest of this paper will be spent discussing the local context and municipal rationale that have led to each of the four approaches, including quotes from municipal workers and informal entrepreneurs. I will also discuss how these policy approaches are used within the context of the city and offer an analysis summarising their effectiveness.

Policy approach 1: Training informality

> T: The majority of home-based entrepreneurs are poor, so they start from their previous experience… but few people have the skills to produce (more profitable) things… They don't start with a market analysis, identifying the demand and (then) acquiring knowledge. There is a lot of competition in particular activities, so profits are small.

National leader, National Federation of Home-Based Enterprises

As the above quote exemplifies, informal enterprises are disproportionately comprised of those with the lowest levels of formal training and education, thus stalling their prospect of economic growth. My survey of HBEs confirms that, in more than 70 per cent of cases, these entrepreneurs entered into their primary economic activity due to their pre-existing skill set, meaning that many find themselves locked into nationally declining sectors (for example, shoe and clothing production in Chile) or economic sectors that face high competition (such as retail activities), threatening the profitability of these businesses from the outset. Even when they decide to move to less congested economic sectors with stronger prospects, many lack the required skills to do so efficiently.

The following quote describes the pitfalls that many informal enterprises face due to their lack of administrative training:

> (An HBE) normally consumes its own working capital two or three times over its lifetime… They do not incorporate all costs into their prices, such as their own labour, or electricity or gas bills… This is one of the main reasons that the most precarious HBEs fail: they eat themselves. They start a corner store and eat the products (from the shop), regardless of whether they are making sales or not.

Public officer, Municipality of Santiago

This inability to properly separate household and business expenses, and an endemic undervaluing of products, creates a cycle where the business consumes its working capital, fails and the entrepreneur must restart from scratch. Here, an entrepreneur in Santiago describes just how long-winded the process of developing business and administrative skills can be when relying entirely on learning naturally over time:

> For years I wasn't breaking even – never!… But I thought that I was making money… With experience, you realise: 'I'm doing badly, I don't make enough'…(and) you start calculating all your inputs.

Hairdresser, Lo Prado

Current actions in Santiago de Chile:

The Municipality of Santiago has created an "entrepreneurship unit", which provides direct basic training and establishes partnerships with universities, institutes and NGOs to provide more advanced training programs to HBEs. The provision of vocational training has been particularly relevant in allowing HBEs to disengage themselves from declining or congested markets, and helping them to move towards more commercially viable activities. Training in administration and marketing techniques has helped entrepreneurs in Santiago to reach a sustainable price system that accounts for their full production costs, and ultimately enhances the sustainability and profitability of their enterprises. Additional training is also provided in e-marketing and technical skills.

Analysis:

The enhancement of human capital in the IE has a direct positive impact on enterprises of the poor, creating a self-enforcing cycle of higher incomes, higher saving and investment capacities and improved working conditions – meaning more "decent work". This type of support effectively provides no fundamental dilemma – an increase in training skills provided to a vulnerable population can be seen as an objective in and of itself, leading to higher overall economic growth and a reduction in public sector dependency. Training programmes ought to be implemented within both national and local contexts, adapted to the specific skills required within each informal sub-sector. The current programmes implemented in Santiago Municipality are limited to home-based enterprises, but a wider scope of programmes would be beneficial as many of the skills taught could be adapted, or are directly applicable, to other informal sub-sectors. Programmes should be offered at little or no cost, as many poor families would be excluded from entering in courses if they were forced to make a trade-off between investing in training and meeting a survival-level income.

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Policy approach 2: Capitalising on informality

> I store (waste) here at home… There is no more space, it's full, so I have to sell (to middlemen) in small quantities at lower prices… I could get better prices by storing large quantities and selling directly to large (recycling) companies. But (to do this) I'd need to have a bigger space and I don't have the money for one. That's the main factor that stops me from growing.

Waste-pickers, Pudahuel

The most common barrier to the growth of informal enterprises across the sectors in my analysis is falling into a "capital poverty trap" that prevents an increase in their production capacity. This is the consequence of a dependency on investment from scant personal savings, loans from an equally poor family or relatives, and low access to credits, often with high interest rates. Furthermore, those who establish an enterprise while living in poverty have access to only the most basic work equipment. These factors inhibit the capitalisation of these enterprises, even when the entrepreneurs can see an economic opportunity and would otherwise be able to seize it and so escape their poverty trap.

Although the private banking system has increased the availability of credit to poorer people, this credit is typically high-interest and provides only a very limited amount of credit:

> It is difficult for (informal workers) to get access to micro-credits as they do not have papers that prove the existence of their enterprises… When they receive credits, the interest rates for small and micro-enterprises are extremely high…on average around 29 to 40 per cent…

Public officer, Municipality of La Reina

At these rates, only a small proportion of high-productivity and highly profitable enterprises can afford to take out credit, while the much larger number of mid- or low-productivity entrepreneurs – typically those from a poorer background – are excluded from the system.

Current actions in Santiago de Chile:

The municipalities of La Reina and Peñalolén have undertaken action to increase the capital levels of local waste-pickers by providing them with tricycles, tools and uniforms. Peñalolén additionally provides local permits of certification for waste-picker enterprises, facilitating their access to bank credits. La Reina Municipality has provided the local waste-picker cooperative (CREACOOP) with a recycling centre, as well as co-funding investment in recycling trucks. CREACOOP has thus been able to collect better quality material in larger quantities, and receive higher prices per kilo as they sell pre-compacted material directly to the larger recycling enterprise without intermediaries.

The Municipality of Santiago provides what it calls "zero-interest credits" for HBEs. To achieve this, governments cover the interest costs of private credits while informal entrepreneurs cover the capital cost:

> Instead of providing one million pesos [USD 1,613] to invest in capital, we cover one million pesos' worth of interest. With this, for every million (that we provide), HBEs invest five million in their enterprises… Reducing the cost of financial access can boost microenterprise productivity, and has an impact on job creation and income levels.
>
> **Public officer, Municipality of Santiago**

As well as making credits available to the poorest self-entrepreneurs, this strategy also massively leverages and so maximises the injection of capital into informal enterprises as public and private financial resources are pooled together.

Analysis:

My statistical analysis substantiates this idea that the direct provision of capital from governments to informal enterprises – from its simplest form, such as the provision of tools to waste-pickers, to higher investment schemes such as the creation of recycling centres – can lead to dramatic increases in the productivity, salaries and working conditions of informal self-entrepreneurs. These provisions should thus be incorporated as part of the development policy toolkit. The zero-interest credit schemes provide an excellent means to foster further growth for an established enterprise that already has access to credit. This allows these businesses to reach their "next level" without being hampered by a growing stream of interest debt, while still holding them accountable for repaying the loan in full and thus demanding financial responsibility. Support for the capitalisation of informal enterprises can thus be a huge contributing factor in the promotion of decent work for the poor.

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Policy approach 3: Broadening market perspectives

Although there is growing number of the type of policies discussed above that focus on increasing the production capacity of informal enterprises, a much less-discussed subject within policy circles is the struggle of enterprises to access a wider or deeper market simply to sell their products, regardless of their output level or product quality. This limited market arises as the result of exclusion from public space and central urban areas, and so entrepreneurs often sell their products from home.

> Micro-enterprise markets are normally limited to their own neighbourhood… Their profits depend almost exclusively on the neighbourhood's economic situation.

Public officer, Municipality of Lo Prado

> For years, I just worked through contacts, so people only came through word of mouth.

Hairdresser, Lo Prado

When markets are limited to an entrepreneur's direct social network – generally family members, relatives and friends – the enterprise has access to a reduced number of customers with a relatively low purchasing power. Building a significant portfolio of clients through word of mouth in this way can take several years. When informal workers have the opportunity to sell to larger enterprises, they do so through a large network of subcontractors or middlemen that consume the profits:

> (Selling to subcontractors) is terrible. They want you to give your products away basically for free. They take so much time to pay you, and often they don't even pay at all… They know that you have to bring some money home no matter what.

Producer of garment, Santiago

These various factors create an environment where the poor face a particularly tough challenge in gaining access to a market for their products.

Current actions in Santiago de Chile:

Lo Prado Municipality is currently strongly promoting wider access of informal enterprises to their local market. This municipality has granted local permits to HBEs, allowing them to sell in local street markets, thus providing them with a space in which they can develop their products and sales strategies, and reach new clients. Lo Prado has also gathered informal enterprises into a localised space through the establishment of production fairs and, most significantly, the creation of a micro-enterprise commercial centre. This hub, named Persa Neptuno, is effectively a producer-retail shopping centre strategically located in front of an underground station, where two hundred local HBEs are able to rent a low-cost branch office in a central municipal space.

The municipality has helped informal enterprises to increase their online visibility by providing training and funding for development in e-commerce platforms, including a website that specifically exhibits the work of local artisans and promotes local small-scale businesses, as well as training entrepreneurs in the best means of exploiting social media and search engines. There has also been an effort made

to source products for the municipality itself in small quantities and from local businesses, amongst them informal enterprises.

Analysis:

My research shows that these policies have a positive impact on the market access of informal enterprises and in turn helps them to create decent work. By focusing on providing street market space for businesses in the IE, Lo Prado has alleviated the entrepreneurs' concern of police controls forcing stalls to close and compromising business opportunities while also providing a space with potential access to new clients. This idea is taken even further in the Persa Neptuno productive hub, which has become a localised area of high demand – a place that locals naturally gravitate towards for goods and services. When an entrepreneur from a relatively distant urban location is given the opportunity to conduct business in a centre such as Persa Neptuno, their number of prospective clients increases dramatically. The exploitation of e-commerce platforms offers a further alternative for increasing both the visibility and market penetration of informal products. If governments take the active role of opening up public space and public resources to the poor, increases in productivity in the informal sector could be truly transformed into higher profits and improved working conditions.

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Policy approach 4: Organising informality

Even those informal enterprises that possess considerable levels of human capital, productive capacity and that exist within stable markets, face significant difficulty in expanding beyond their micro-enterprise size. Even the most successful small informal enterprises can struggle to secure the type of large investment – such as purchasing high-tech capital or constructing large infrastructure – that is required to scale up to a medium-size enterprise and expand their profitability.

Consider, for example, the case of the following garment enterprise, where the usage of a small home dwelling as a production and storage space is used as a means of reducing the permanent costs of running the business:

> People say that I have the ability to produce 100 (t-shirts) but I only sell ten… (In fact) I could produce 100 but I only have space for ten. My workshop is too small… I have to reject orders because, where could I put 500 shirts?… I need to expand somewhere else, but our household wouldn't be able to pay the rental costs.

Garment producer, Las Condes

This successful enterprise has quickly reached a point of overcrowding inside the home space, and business expansion would require either paying high rental costs or purchasing a new space, both options beyond the business' margins of profitability and tolerance to risk.

In an attempt to overcome these limitations, the current trend within informal enterprises is an increase in organisation and, particularly in the last decade, a movement from a union-type organisation that demands rights for informal workers, towards cooperatives or horizontal networks of self-entrepreneurs that work together in the pursuit of productivity objectives. Cooperatives exist as legal structures that link multiple informal entrepreneurs, allowing them the benefits of collective negotiation with public institutions and private enterprises, and providing a way to pool investments with which they can develop infrastructure and purchase costly machinery.

> Being in a cooperative has been fundamental to getting this piece of land… To be able to sell to (large recycling) companies you need large quantities…such as a container with three to four tonnes of paperboard three times a week… Without our land, we wouldn't be able to sell to large enterprises – we would have had to keep selling to a middleman.

Waste-picker, La Reina

Alternatively, a "horizontal network" type of self-organisation has led to clusters of informal enterprises growing in specialised neighbourhoods. In a similar way to the Persa Neptuno discussed in the previous section, this allows the businesses to increase the aggregated demand for their products. However, rather than attracting customers to a well-located "skills hub", this less-structured approach draws people to lower-income areas where they would often not normally venture, thus breaking the spatial trap of enterprises in poorer locations. A public officer explains the natural progression that leads to these horizontal networks:

> (Informal HBEs) understand that they're in a trap – that they need to pool capital and attract clients… One solid example is 'El Mall Chileno'… They started with workshops (at home) and now they have a sales point in their own mall… They are clothing producers who…

> searched for a market together, who buy inputs in large quantities and get credits together. They even built a five-storey building…that attracts hundreds of people to the area every day… They received a credit of 5,300 million pesos [8.54 million USD].

Public officer, Santiago

Current actions in Santiago de Chile:

The municipality of Peñalolén has helped to organised a cooperative, the Association of Micro-Entrepreneurial Recyclers, who are able to make use of "green collection points" where neighbours bring pre-sorted recyclable materials, and who then sell this material collectively. Alongside this, Macul Municipality has offered to support street vendors who are willing to increase their levels of organisation. These street vendors were able to receive a commodatum for public spaces to build two covered street market – *Ferias Modelo Juan Pinto Duran* and *Quilin* – along with investment in potable water, electricity, public toilets, green spaces and a children's playground. The street vendors remain fully responsible for cleaning the area and providing parking space for clients.

Analysis:

The existence of cooperatives and horizontal networks has been of great importance for informal enterprises, allowing them to grow their businesses significantly. The collection points exploited by the aforementioned micro-entrepreneurial association in Peñalolén allow the waste collectors to obtain higher prices per kilo. Thanks to the shared profits of CREACOOP, the waste-picker cooperative of La Reina, the group has been able to purchase two waste lorries and processing machinery, which has created an overall increase in the quantities that they collect. This

cooperative is fully legally constituted, and workers are contracted with monthly hours and receive a guaranteed salary, and also contribute to health and pension schemes.

The clustering of street vendors that has occurred in Macul has increased their capacity to attract out-of-neighbourhood clients that travel by car to poorer areas. The provision of electricity and clean water has allowed street vendors to sell more profitable products that require refrigeration or processing, such as natural juices, ice cream and frozen food. Operating a street market under cover also means that stalls can operate on rainy days and receive higher amounts of foot traffic, as they are preferable to uncovered markets at these times. The members of this organisation have not only obtained higher profits, but have considerably improved their working conditions.

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Governmental action supporting the organisation of informal entrepreneurs yields results that ultimately increase capitalisation, demand, salaries and improve working conditions for the enterprises of the poor, once again creating more decent work for the lower end of the labour market.

Conclusion

Beginning with a recognition that the informal economy is here to stay, this report has argued that the fight to promote decent working conditions on a global scale must incorporate developmental agencies and governments that embrace and support the informal economy. Rather than fighting informality, these bodies must move towards an approach that builds on the informal economy's inherent capacities.

The paper has highlighted that the low productivity, low salaries and the resulting poor working conditions within the informal economy are the consequence of four poverty traps – lack of human capital, precarious production capital, a lack of access to potential sales markets and a lack of larger-scale organisation – that are typically faced by the enterprises of the poor. Governmental support for informal enterprises is the necessary path to take to break these poverty barriers and ultimately promote decent work.

Governmental support for informal enterprises is the necessary path to take to break these poverty barriers and ultimately promote decent work.

A wide variety of effective governmental interventions outlined above contribute to the realisation of this goal. These measures can be direct and tangible, such as the provision of financial aid or administrative and managerial training, or broader and less concrete, such as the improvement of enterprises' access to markets or fostering organisation within the informal economy. All of the highlighted interventions work to increase financial independence and sustainability, while allowing poor entrepreneurs to break free from their initial state of poverty and determine a positive future for themselves and their businesses. When striving to promote self-determination and economic growth, governments are in turn striving for the creation of decent work.

Supporting the informal economy requires radical change in both the mindset and practices of policymakers, moving towards an attitude that recognises that the informal economy is the consequence and not the cause of poverty. Because of the social value and huge potential offered by

an approach that supports the efforts of poor entrepreneurs to improve their own livelihoods, it is essential that more positive policies towards the informal economy emerge in the future.

> I'm going to tell you my dream… The state asks: 'What would you like to do?… We are going to work beside you, we're not going to leave you on your own, and we'll tell you why you have failed: you did this wrong, let's try this instead'. I mean, guiding you. Because to become a big enterprise, you need state support, the state needs to push you forward a little. Instead, when you start from the bottom, from poverty, the state crushes you… The taxes, the policing, the closures… They destroy your enterprise.

Owner of a fast-food shop, La Granja

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The Institute of Public Affairs
The London School of Economics
and Political Science
Houghton Street
London
WC2A 2AE

Tel: 020 7106 1247
Email: **IPA@lse.ac.uk**
Web: **lse.ac.uk/IPA/Home**